

Economic & Revenue Outlook

Presented to
State Economics Forum
Urban Enterprise Center

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Seattle, Washington



WASHINGTON STATE
ECONOMIC AND REVENUE FORECAST COUNCIL



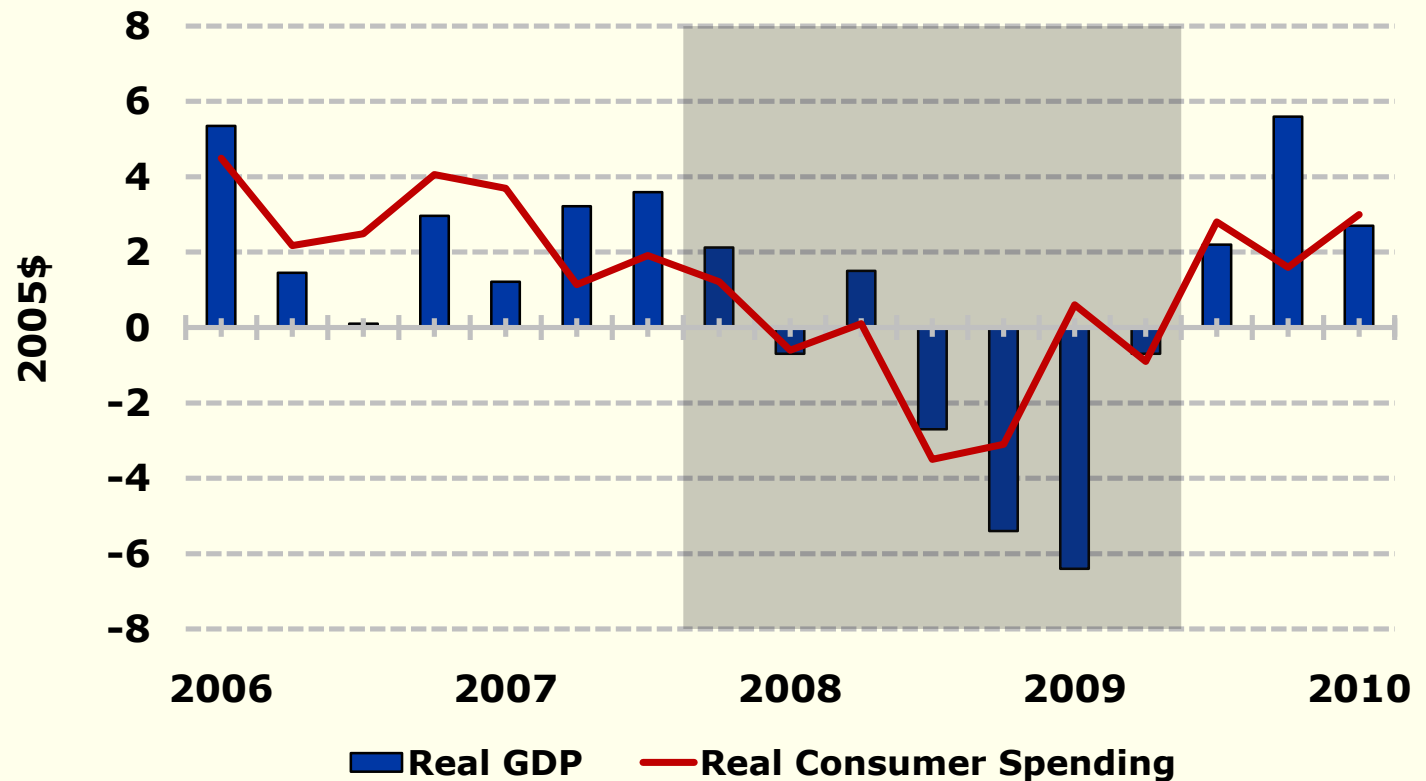
Summary

- There is evidence that the economic recovery stumbled in May – we are now predicting near-term weakness, but a continuing recovery
- The downside risk to the forecast have increased, however
 - Weak employment reports in May and June
 - Weak retail sales report in May
 - Fears of European contagion
- Other risks are the same as before
 - Downside: weak construction; community banks; tight credit for small business
 - Upside: exports; aerospace; software



We have had 3 consecutive quarters of GDP and consumer spending growth

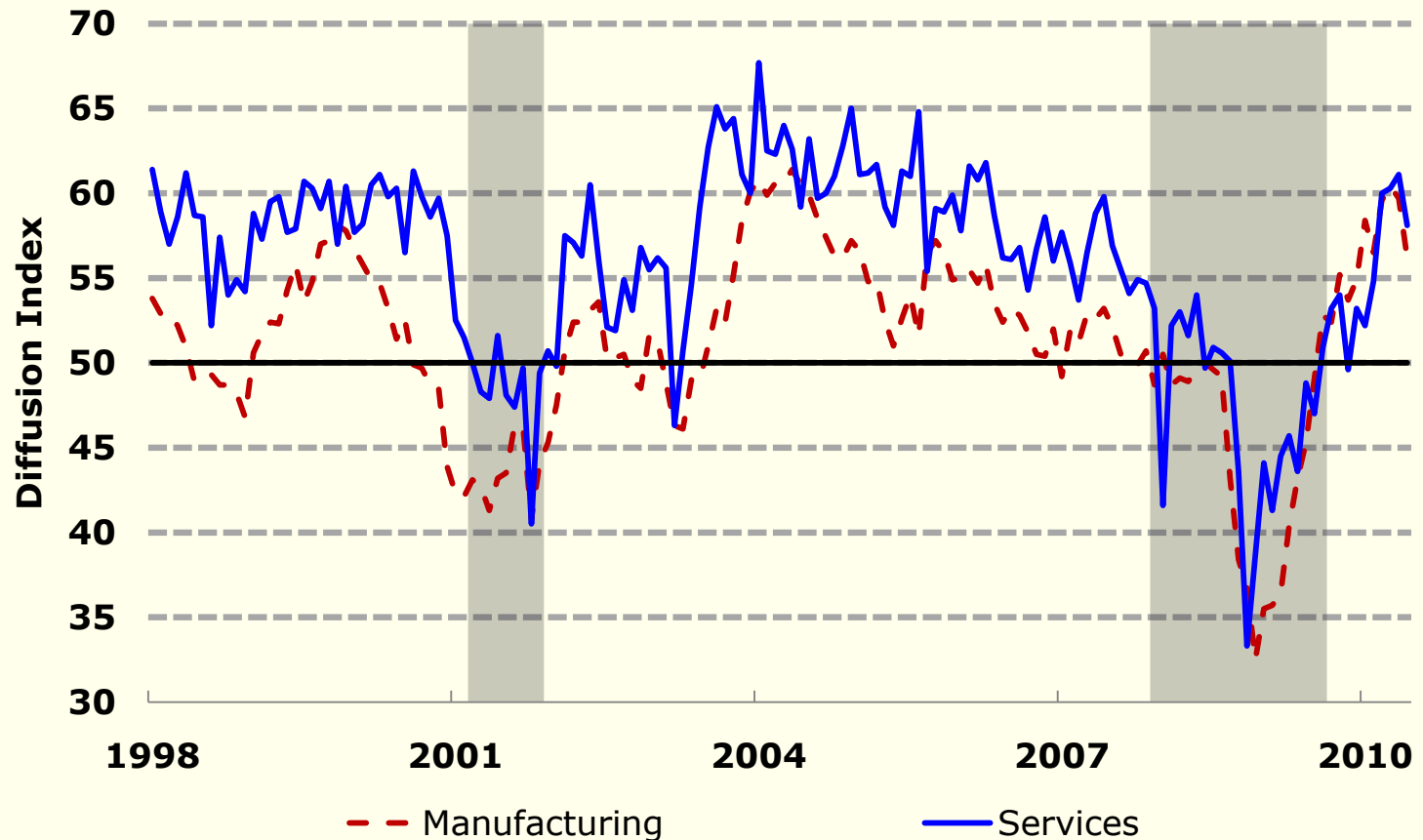
Percent growth, SAAR





ISM indices for both services and manufacturing indicate growth

An index greater than 50, implies growth

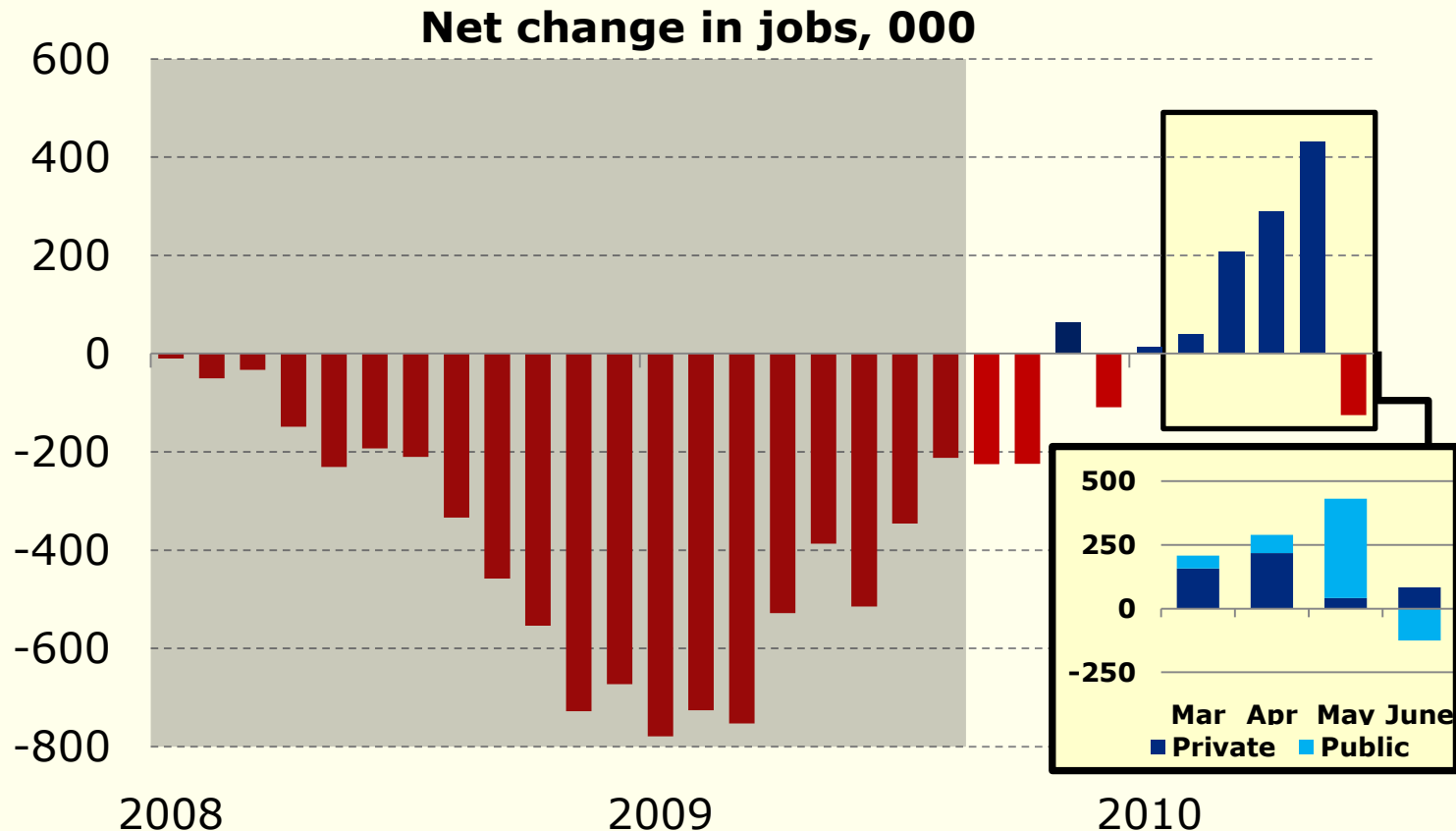


Source: Institute of Supply Management; data through June 2010



The jobs recovery stalled in May, and remains weak in June

Only 33,000 private sector jobs were added in May, down from 218,000 in April



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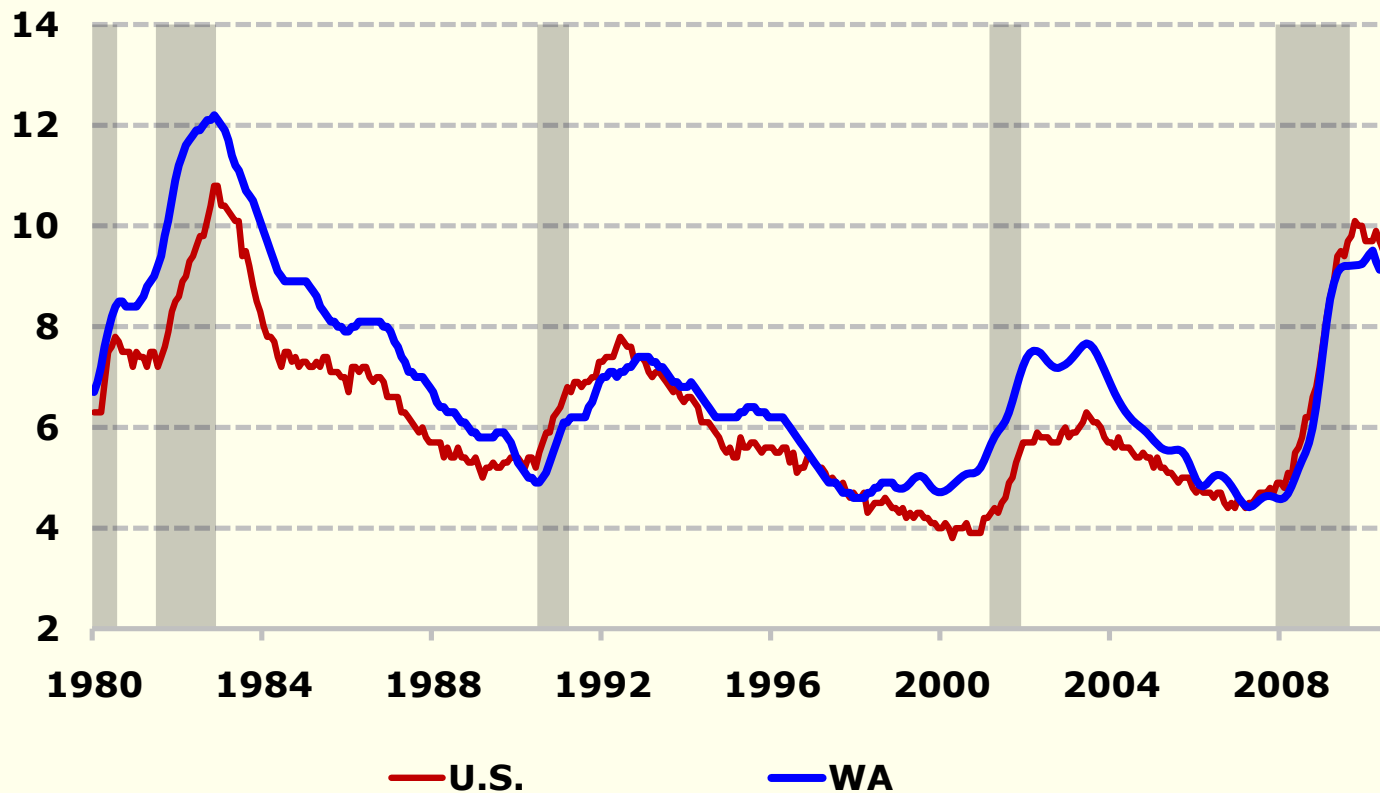
Source: BLS; data through June 2010



Unemployment is still high

It is normal for this rate to continue to rise even after the economy is in recovery

Unemployment Rate, Percent, SA



Source: WA ESD, BLS; data through June 2010

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At this stage in 1981-82, the state economy had made up all of the job losses

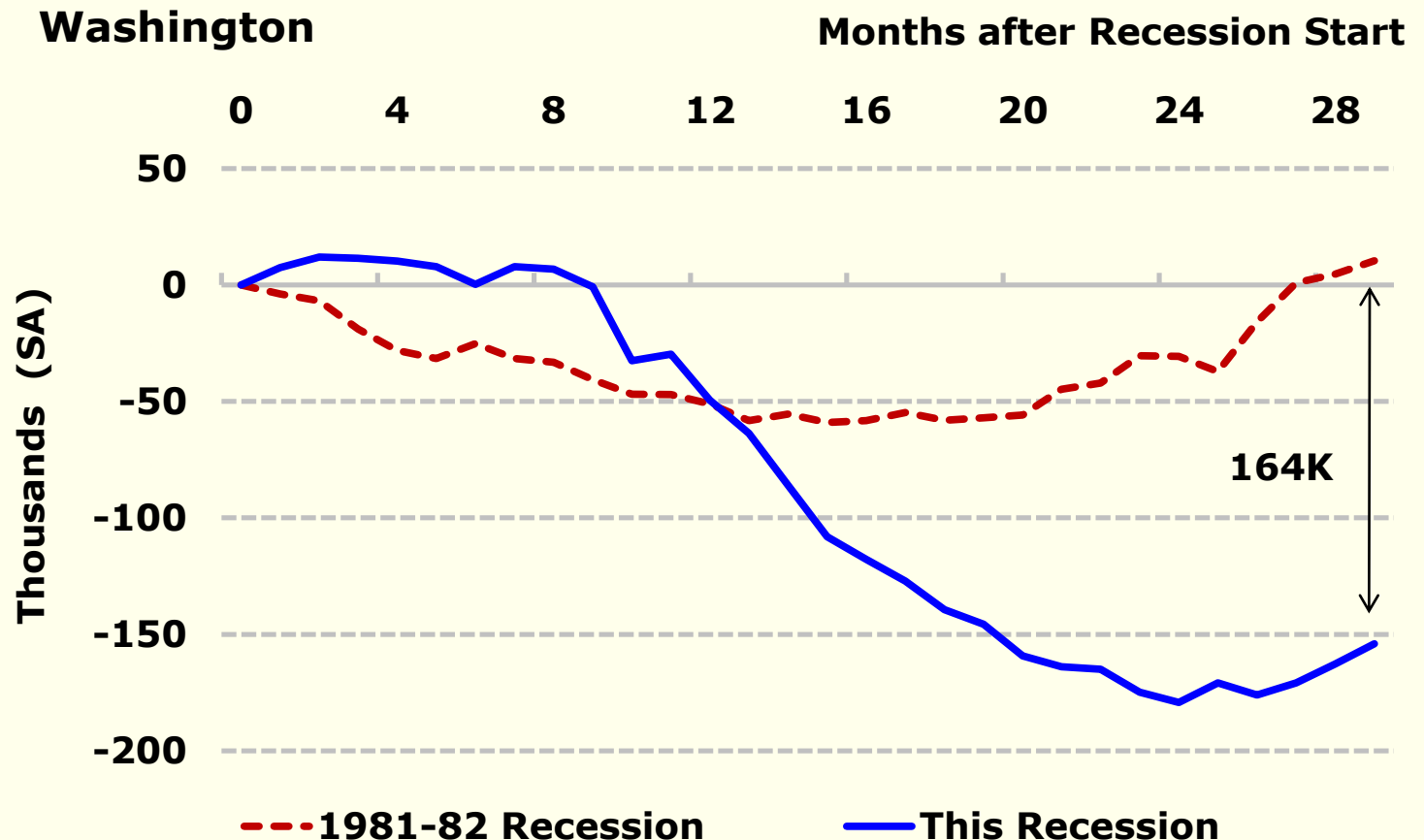
Peak to
trough job
losses

1981-82:

2.9% of
labor force

This time:

5.1% of
labor force



Source: WA State ESD, ERFC; data through May 2010



The S&P 500 VIX volatility index has spiked recently

This index is a proxy for fear and uncertainty in markets



Source: Yahoo Finance; data through July 7, 2010

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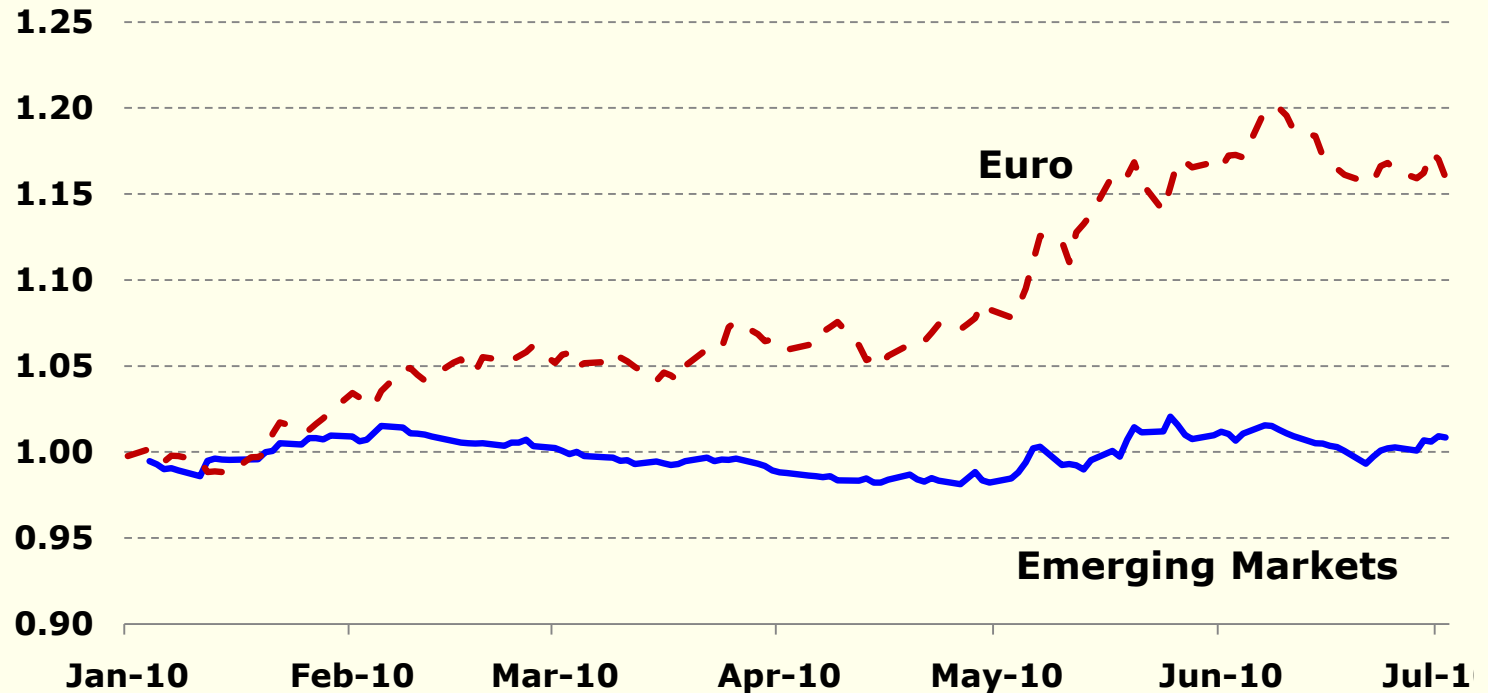
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The USD has appreciated against the EUR this year, but not against emerging market currencies

U.S. Dollar versus select currencies

Index, Dec. 31, 2009 = 1.0



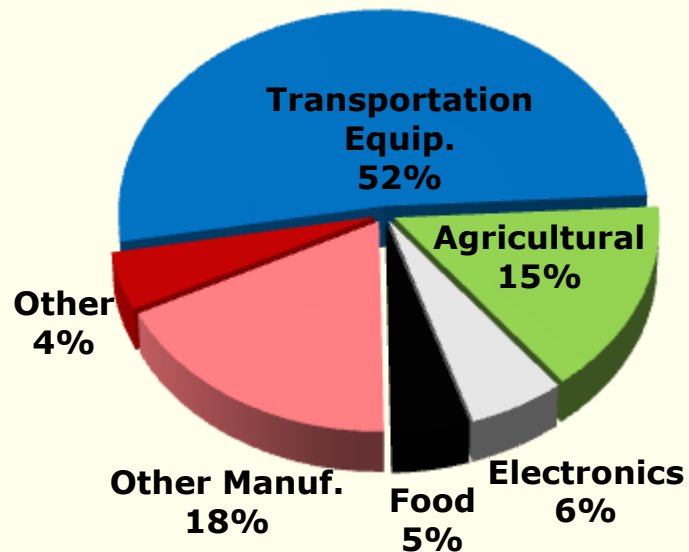
Source: US Federal Reserve Bank, ERFC; data through July 2, 2010



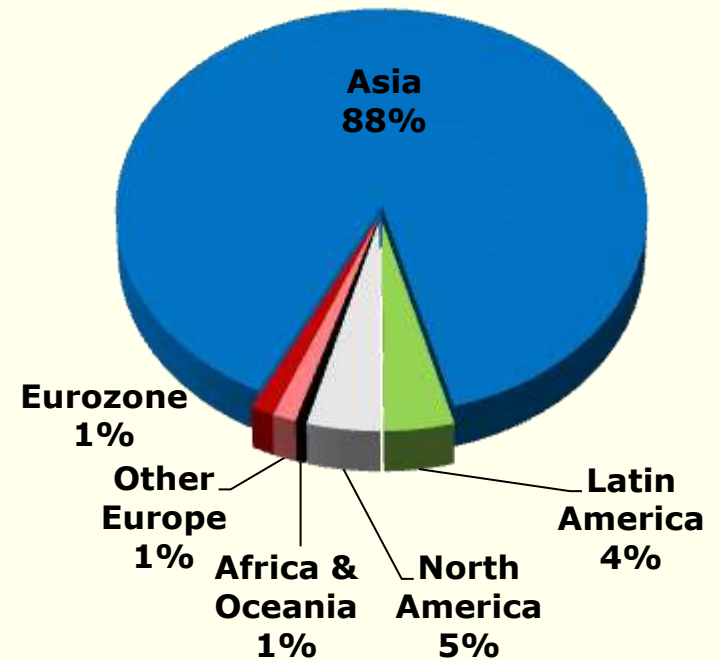
WA exports are less affected by a weaker EUR

2009

Exports By Industry



Destination of Agricultural Exports



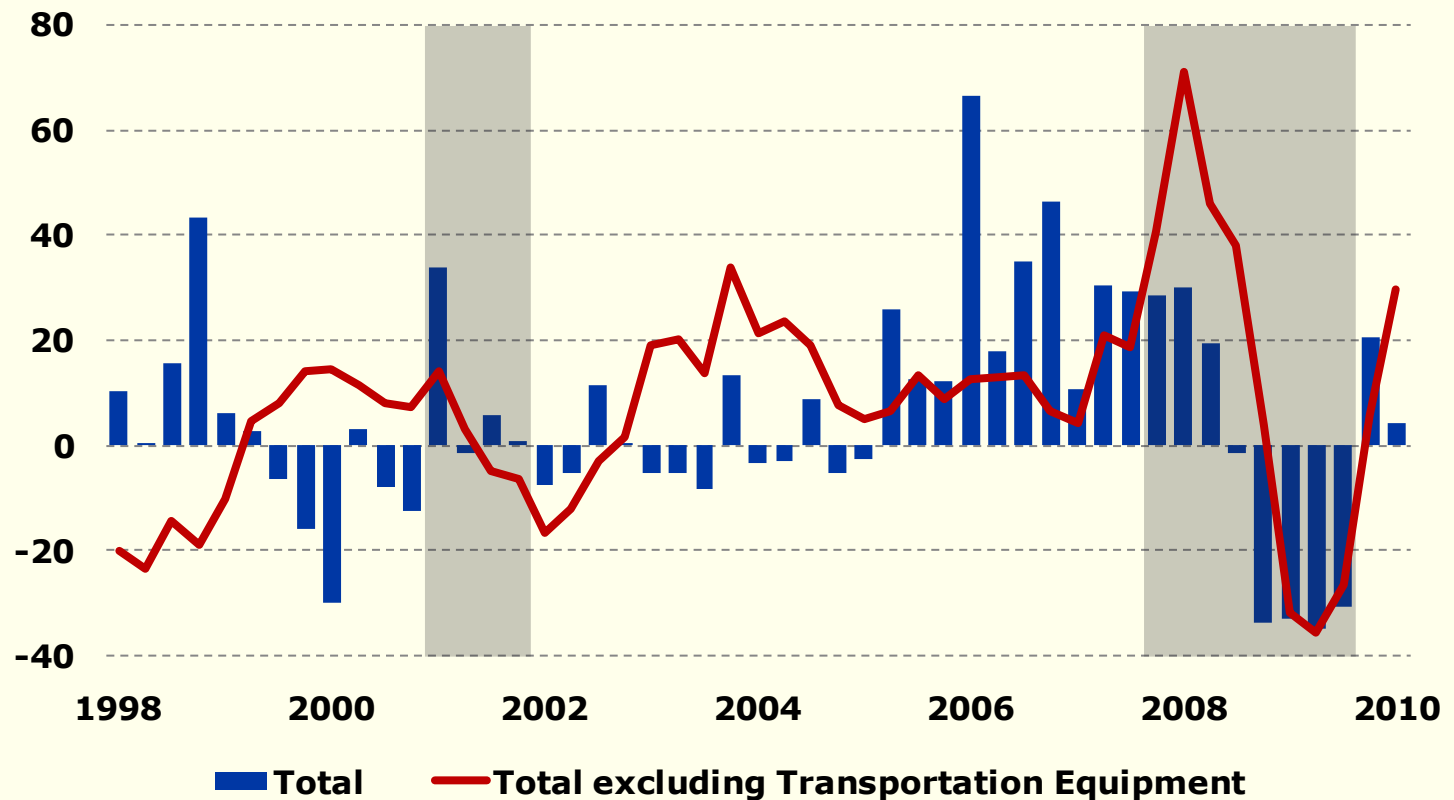
Source: Wiser Trade Data



Exports will help the state recover faster than the nation

Exports excluding transport equipment were up 30% in Q1

Exports
Percent Change, year ago



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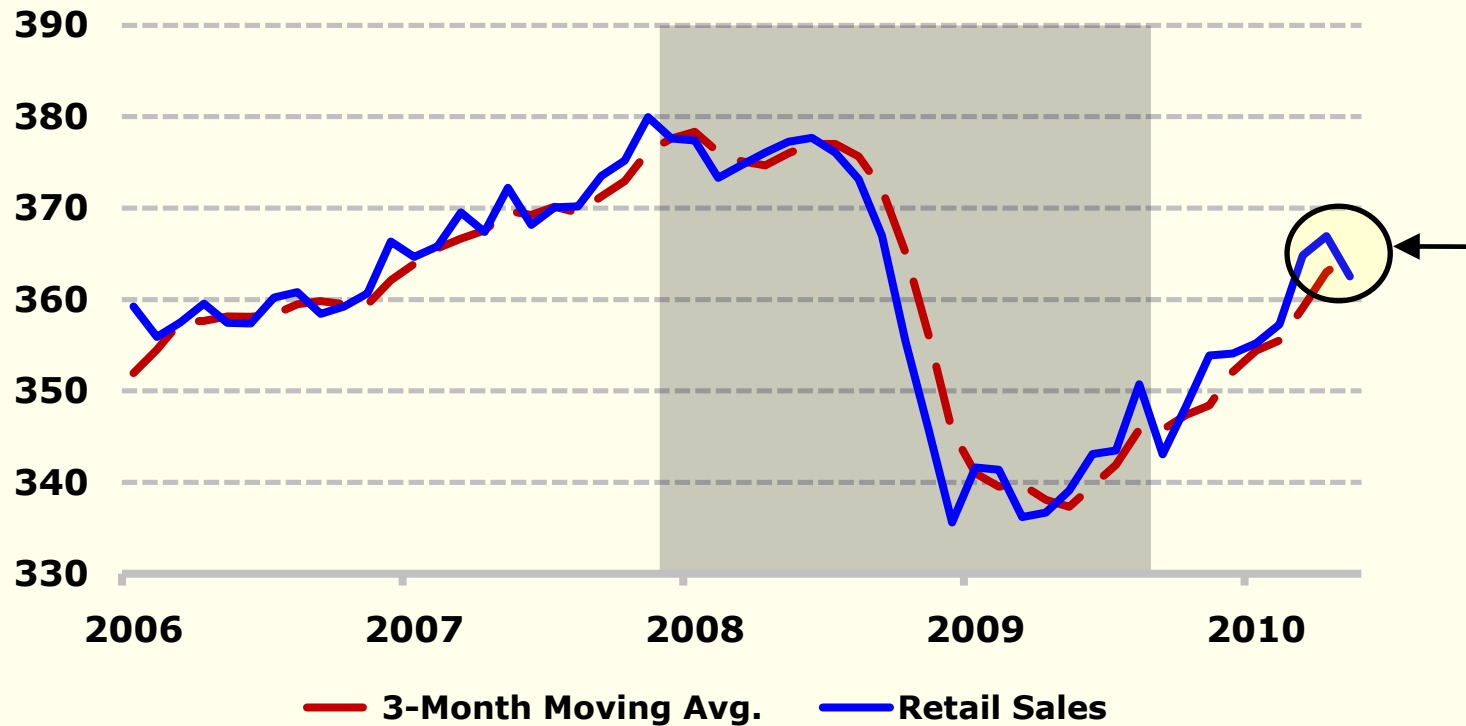
Source: Wiser Trade Data; through 2010 Q1

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Retail sales fell in May

U.S. Retail Sales and Food Services
USD, billions



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Source: U.S. Census Bureau; data through May 2010

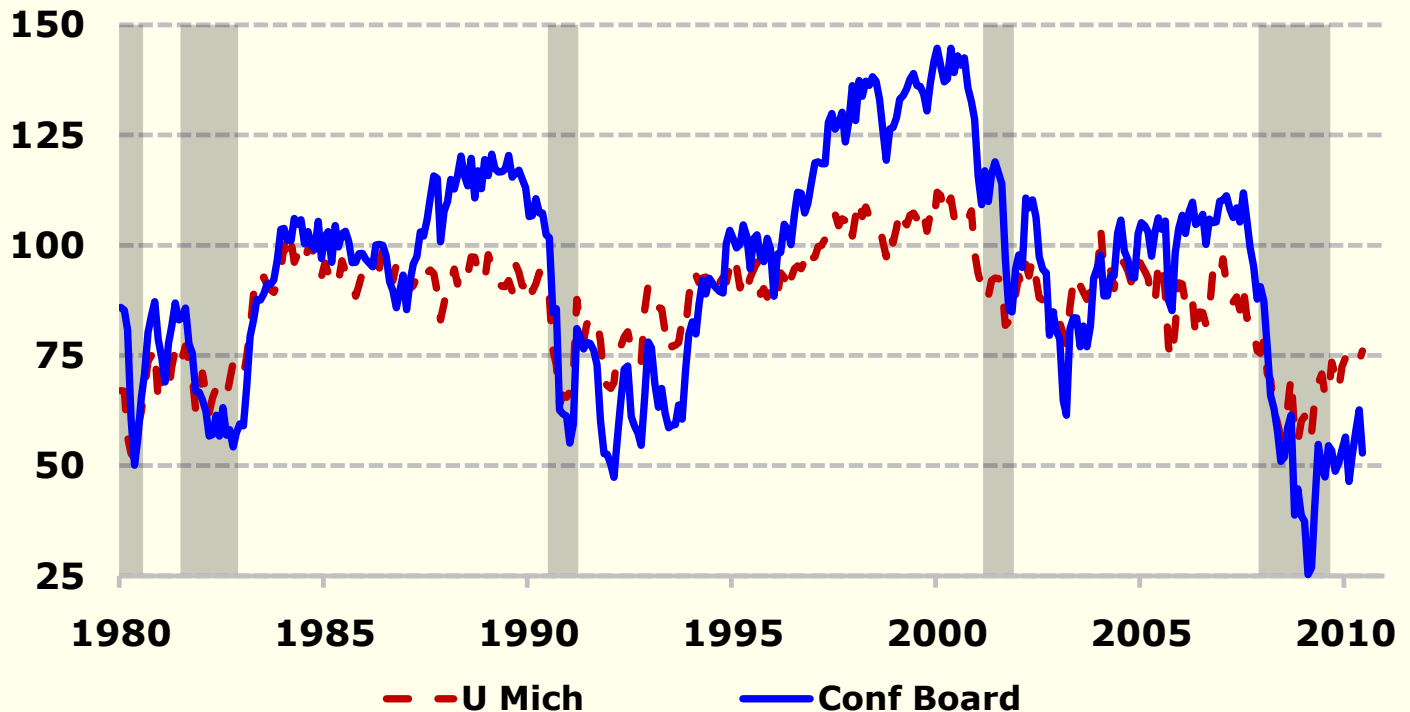


Consumer confidence is improving, but slowly

Index

Mich: 1966Q1 = 100, SA

Conf Board: 1985 = 100, SA



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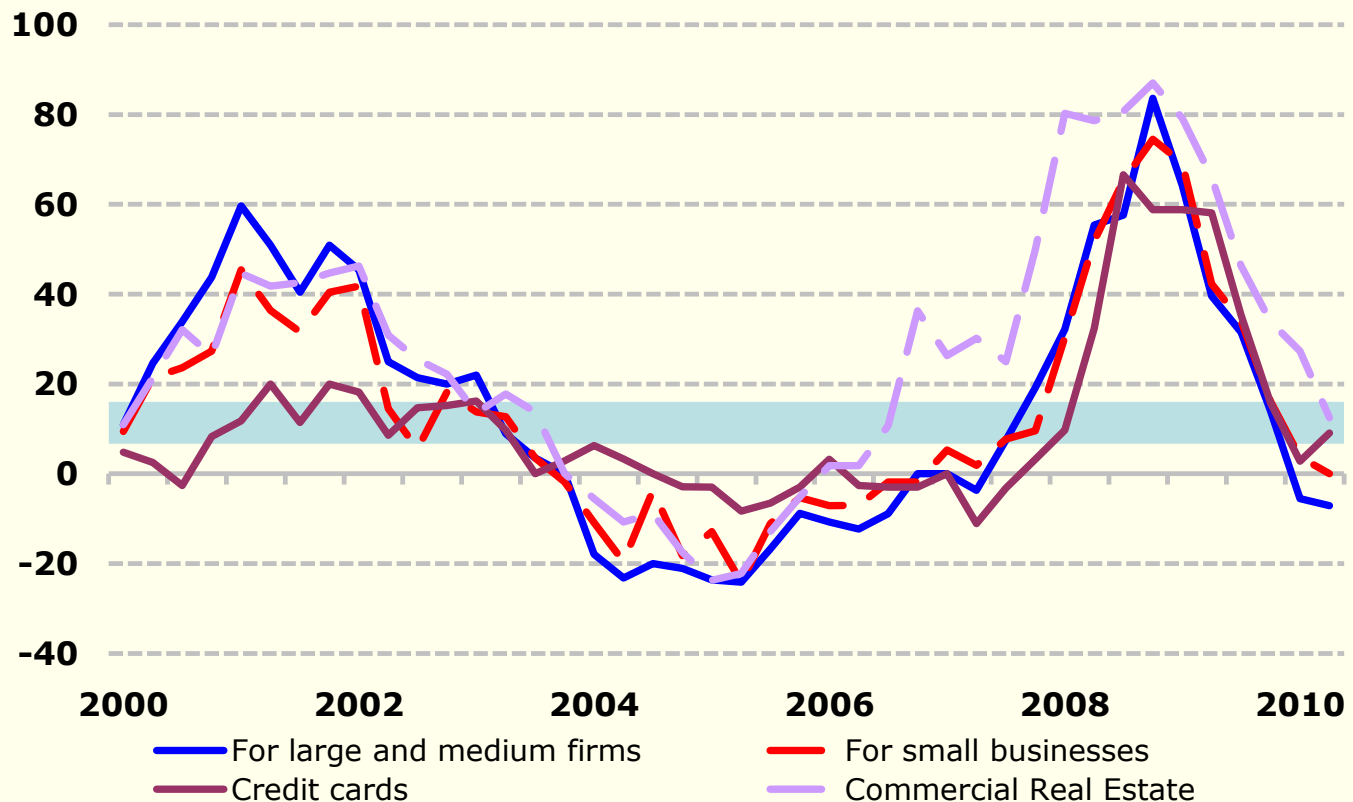
Source: University of Michigan; Conference Board, data through June 2010



Large bank lending appears to be easing

Survey includes 60 large domestic banks and 24 U.S. branches of foreign banks

Net Tightening minus Easing Percent



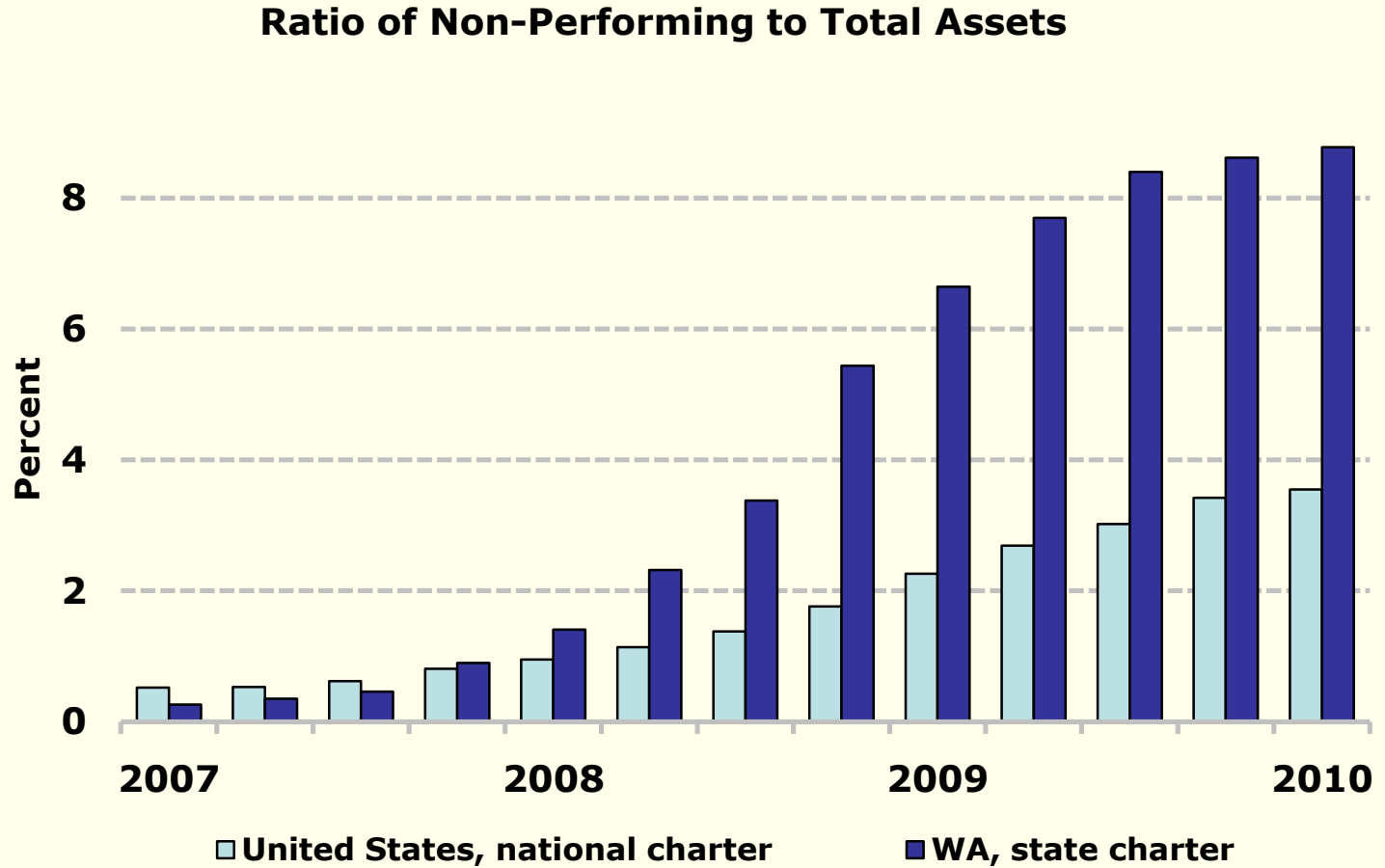
Source: Federal Reserve Board, Senior Loan Officers Quarterly Survey; data through April 2010 survey

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Asset quality of regional banks is poorer, but leveling off

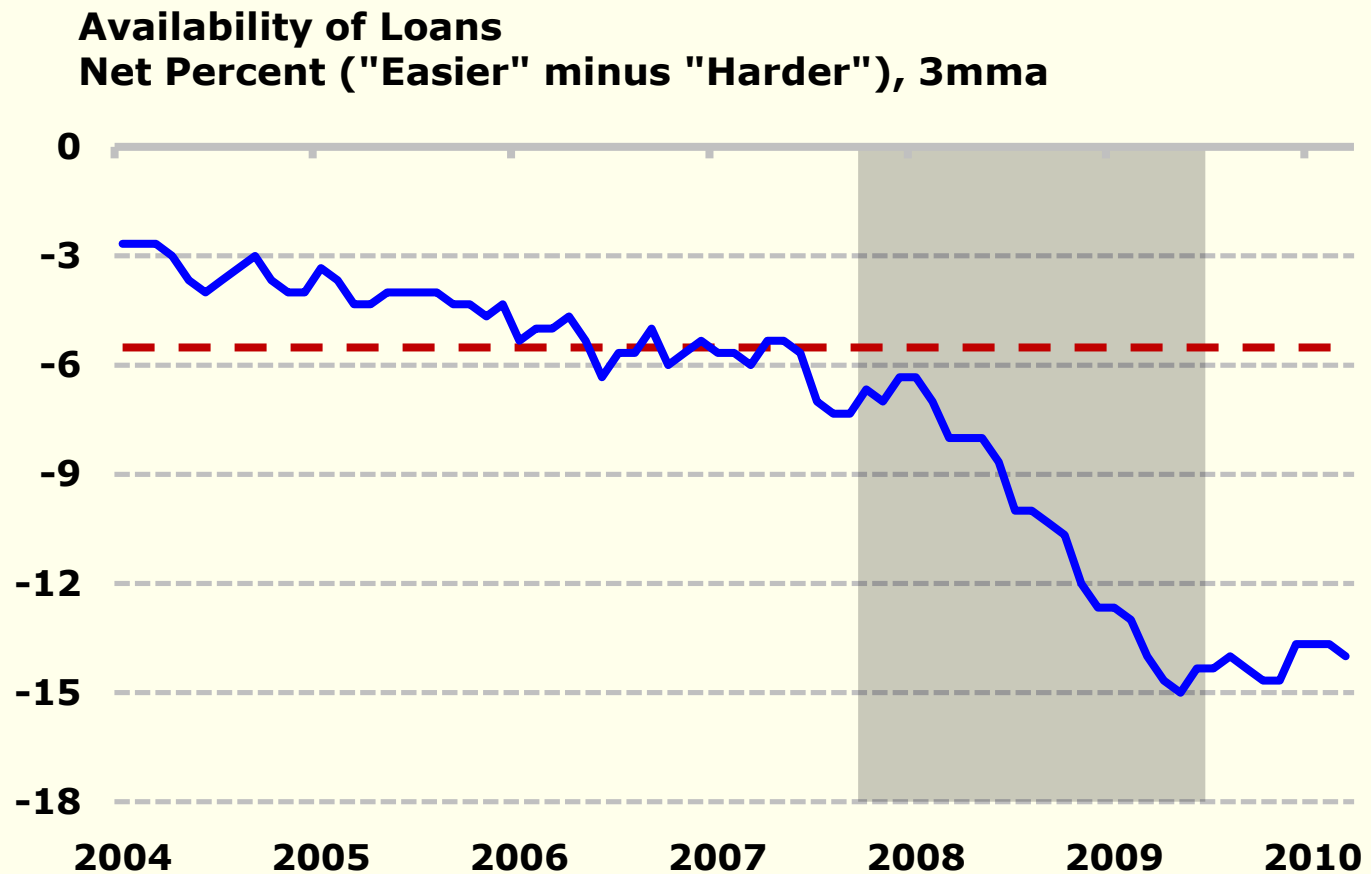
The poorer asset quality of regional banks is due to their disproportionately high exposure to commercial real estate



Source: FDIC, data through 2010 Q1



Credit conditions remain tight for small business



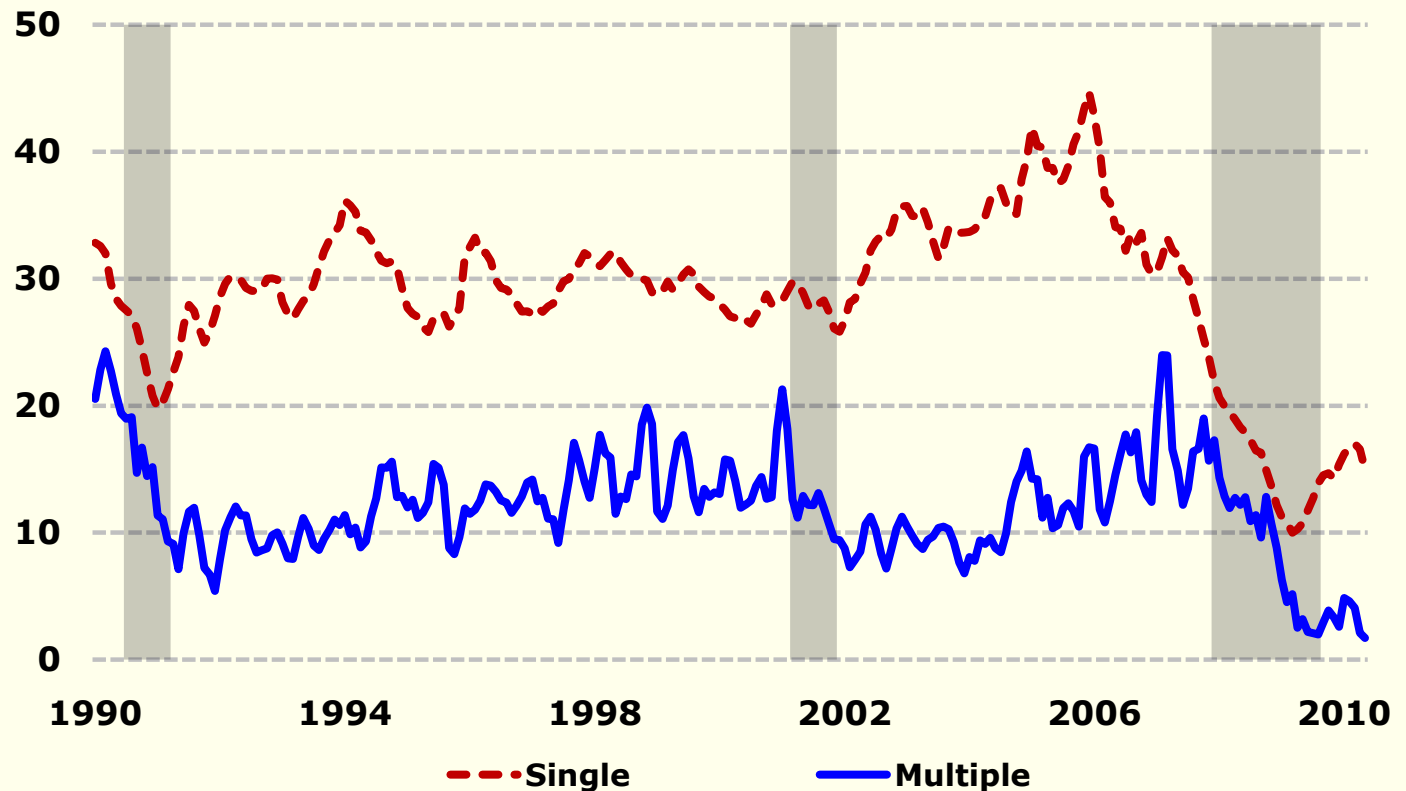
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Source: National Federation of Independent Business; data through May 2010



WA single family housing is expected to flatten out, now that the first time homebuyer tax credit has expired

Thousands, SA, 3MMA

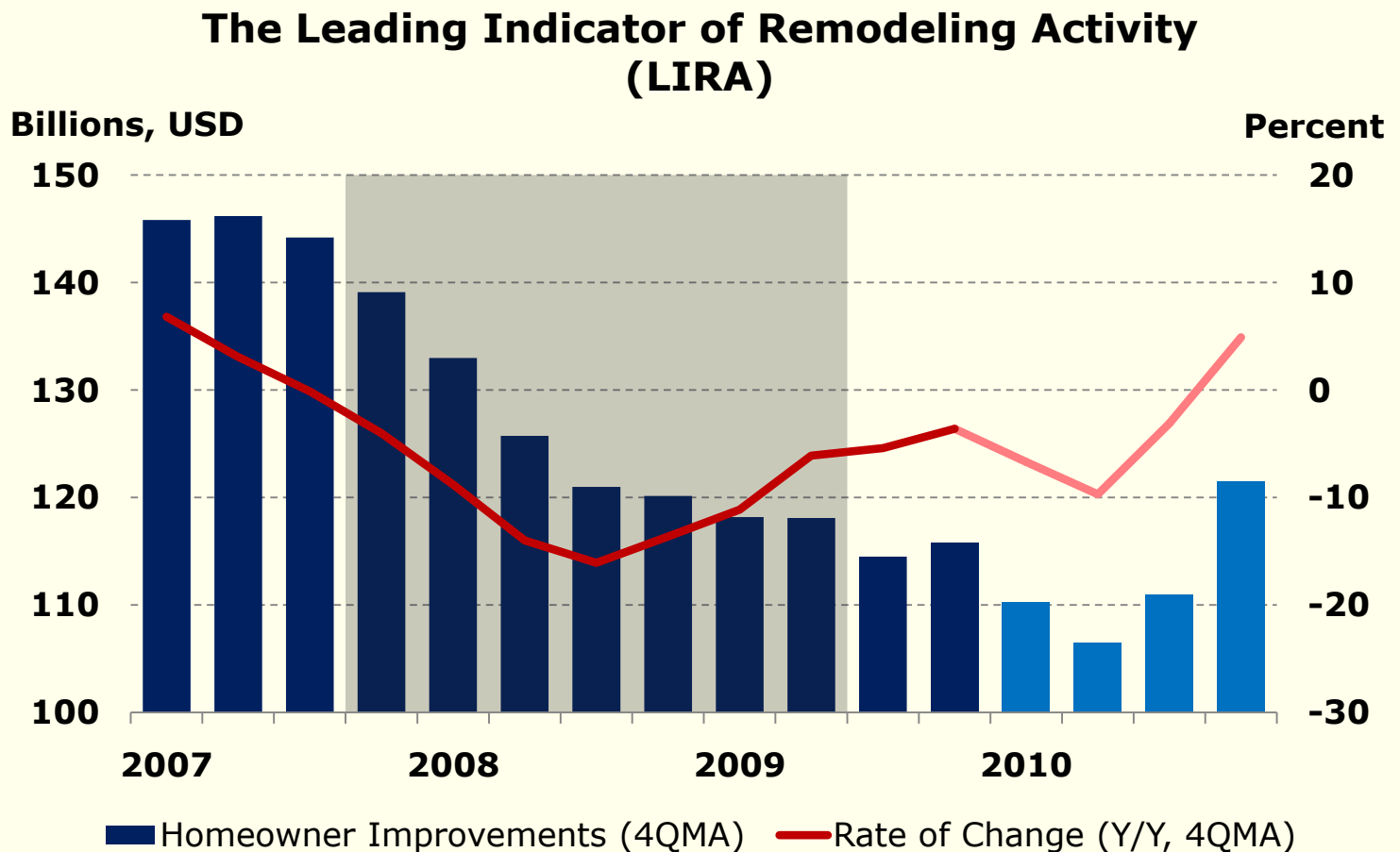


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Source: U.S. Census Bureau; data through May 2010



Leading indicator suggests remodeling improvement in 2010

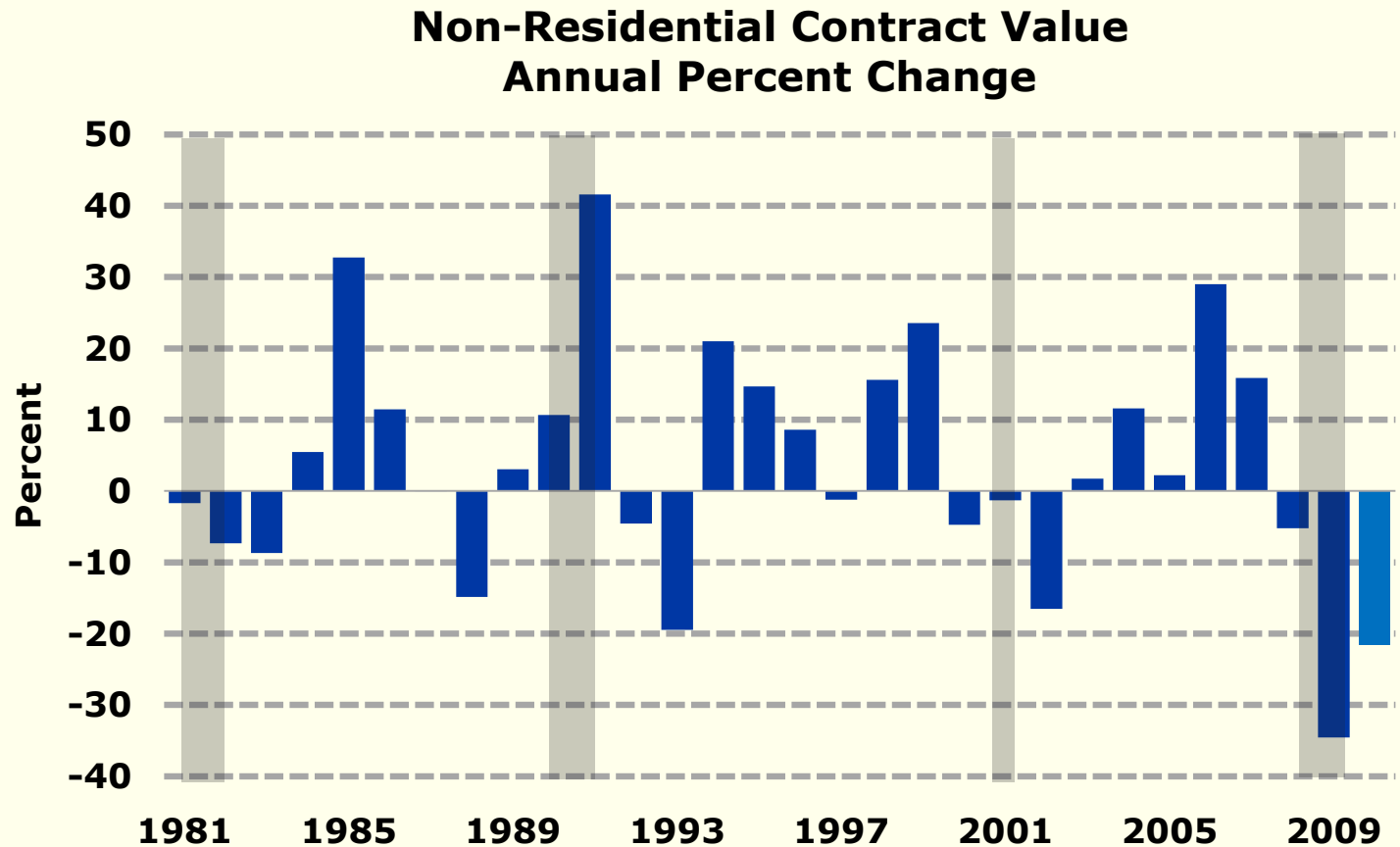


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Source: Joint Center for Housing Studies of Harvard University, actual data through 2009 Q4



This is the worst downturn in non-residential construction in 30 years

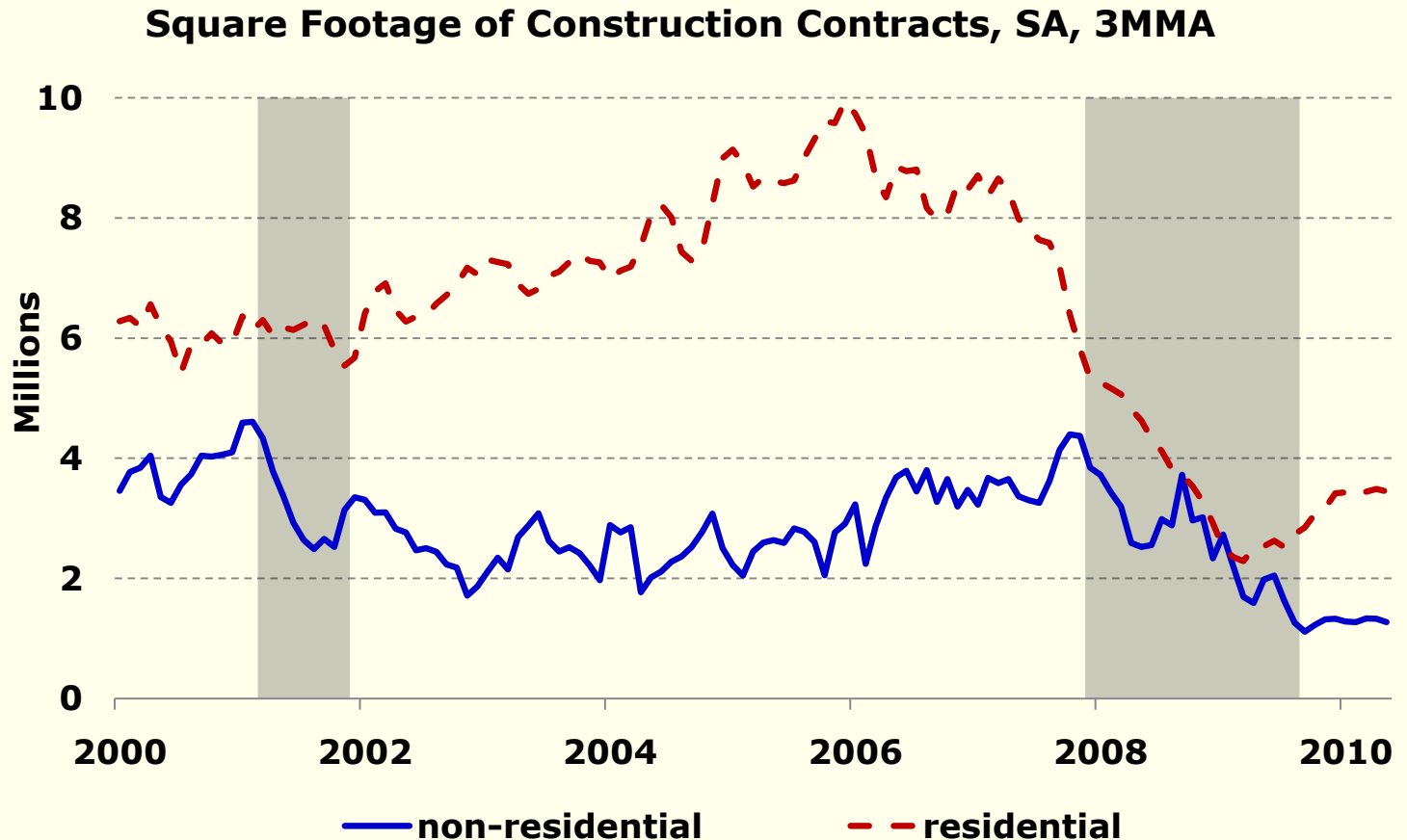


Source: McGraw-Hill Construction, data through May, 2010



New construction in WA is no longer in free-fall, but the recovery will be weak

Residential square feet is up 55% since reaching a trough in Jan 2009



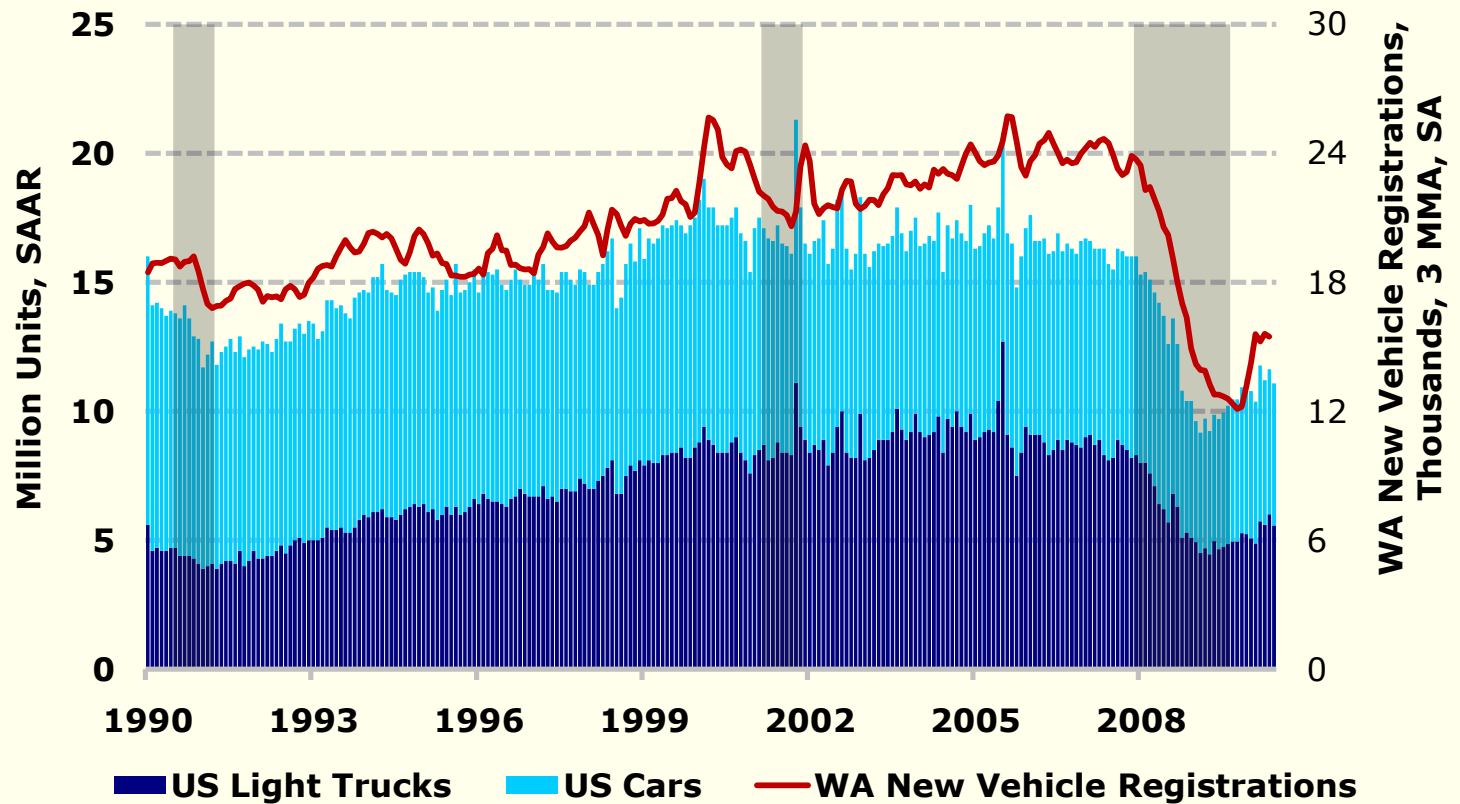
Source: McGraw Hill Construction, ERFC; data through May 2010



Automotive sales continue to improve

National car sales were 19% higher in May 2010 than in May 2009

Cash for Clunkers effect removed



Source: Autodata Corporation, WA DOL; data through June 2010

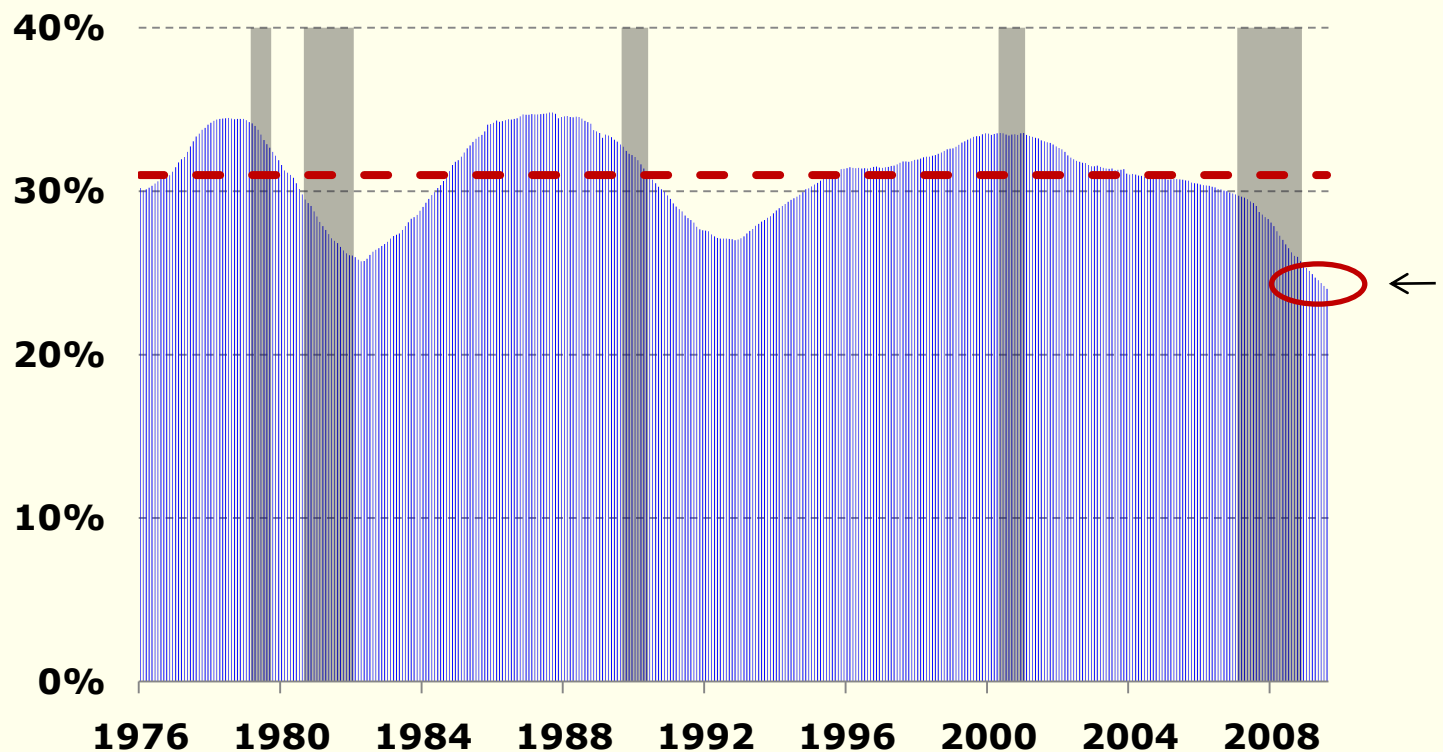
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Relative age of the car fleet indicates continued turnaround in car sales

The percent of "old" cars on the road is at a historic high

U.S. LMV Sales: Ratio of 36/120 Months

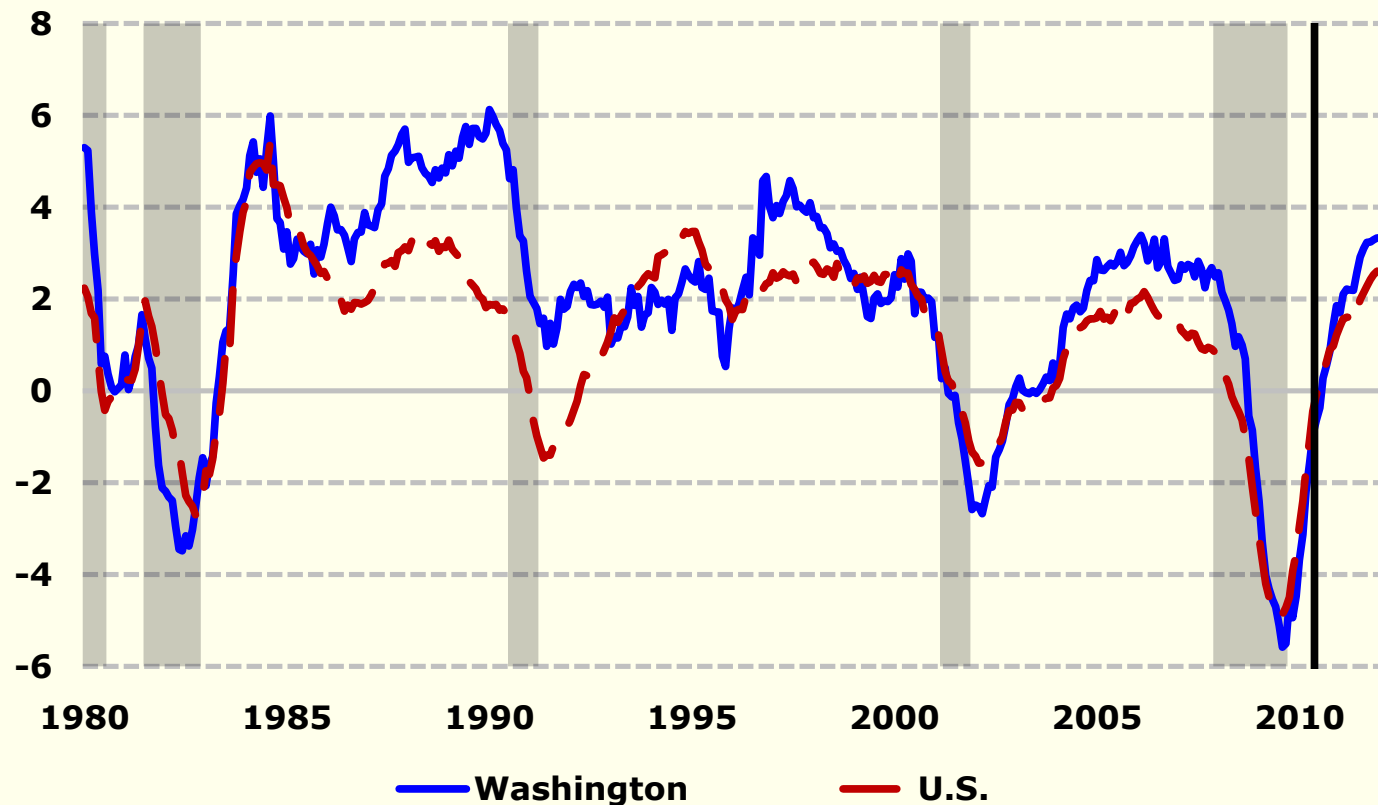


Source: Autodata Corporation, ERFC; data through June 2010



WA employment lagged the nation in the downturn and will recover stronger than the nation

Percent change, year ago

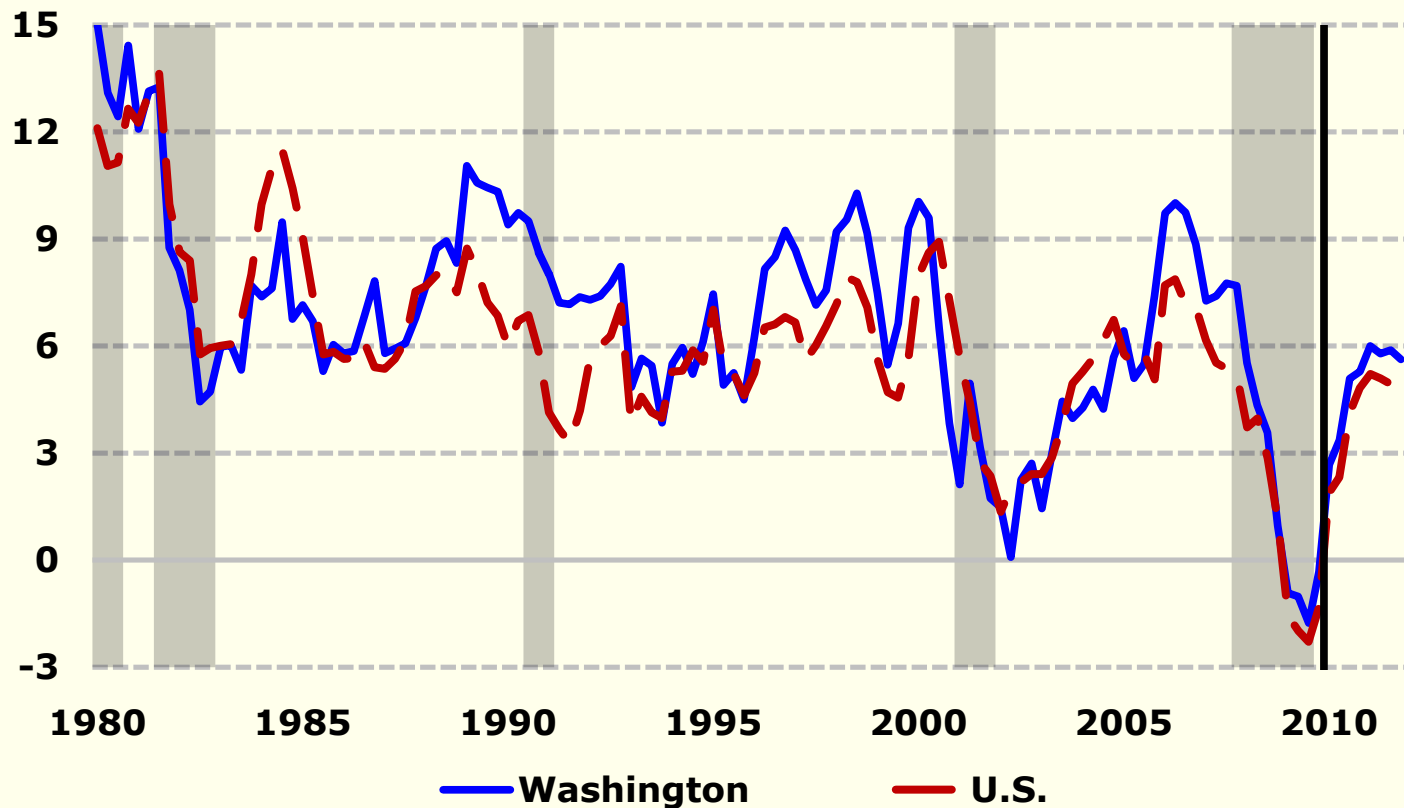


Source: ERFC June 2010 forecast; actual through May 2010



The recovery in WA personal income growth is expected to be better than the nation's

Percent change, year ago



Source: ERFC June 2010 forecast; actual data through 2010Q1



Forecast changes: General Fund State, 2009-2011 Biennium

**February
Forecast:**

**\$28,725
million**

**USD
millions**

June '10 Forecast

	<u>Collection Experience</u>	<u>Non- economic Change</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	(\$34)	\$749	(\$159)	\$27,802	\$556
All other agencies	(\$5)	\$54	(\$47)	\$1,481	\$1
Total GF-S	(\$39)	\$803	(\$207)	\$29,282	\$558

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* Detail may not add to total due to rounding



Forecast changes: General Fund State, 2011-2013 Biennium

USD Millions

USD millions	June '10 Forecast				
	<u>February 2010 Forecast</u>	<u>Non- economic Change</u>	<u>Forecast Change</u>	<u>Forecast</u>	<u>Total Change*</u>
Dept. of Revenue	\$30,658	\$1,556	\$219	\$32,433	\$1,774
All other agencies	\$1,566	\$105	(\$21)	\$1,650	\$84
Total GF-S	\$32,225	\$1,661	\$197	\$34,083	\$1,858

* Detail may not add to total due to rounding

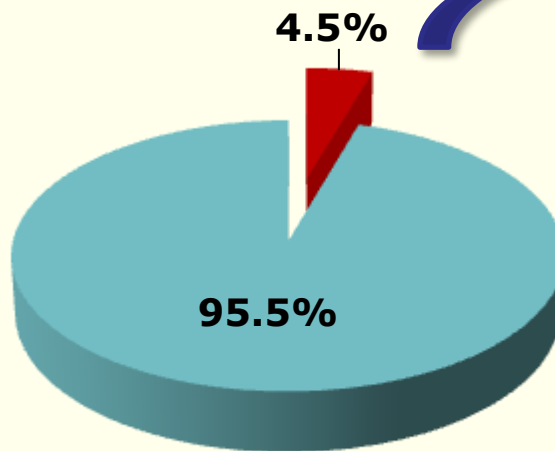


Construction contributes more to the GF-S than to State Product

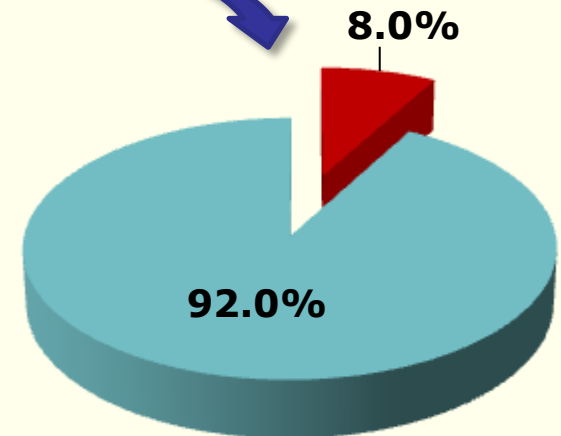
**1997 – 2004
Average**

**Excludes
bubble
years**

Gross State Product



General Fund Revenue



■ **Construction**

■ **All Other**

Source: Bureau of Economic Analysis, ERFC

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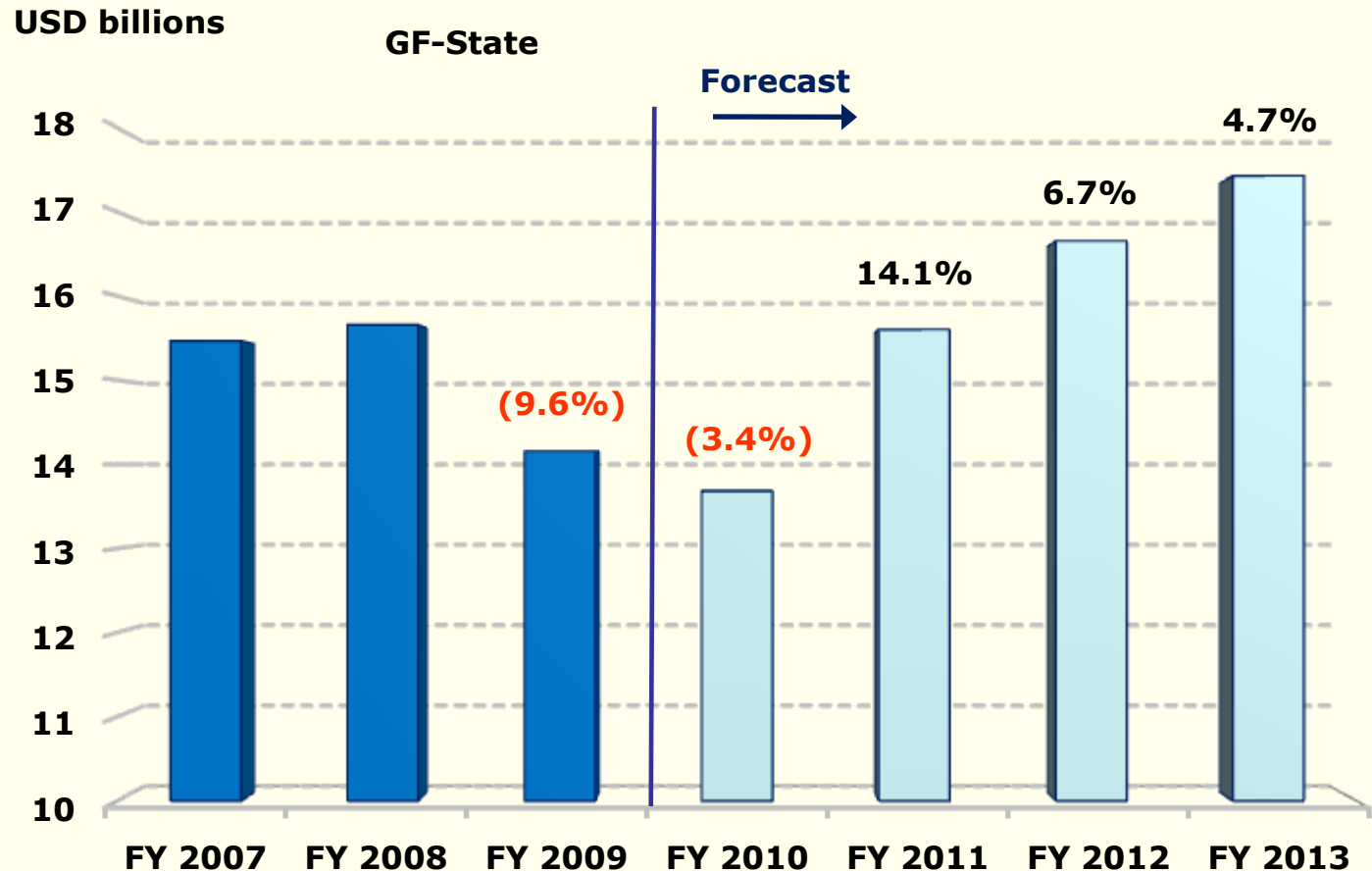


General Fund* forecast by fiscal year

* General Fund & Related Funds for FY 07, 08, and 09

General Fund – new definition, for FY 10-13

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Source: ERFC forecast, June 2010; includes impact of legislative changes



Conclusion

Pluses

- Recovery in progress
- Evidence of pent up demand
- Job growth has returned
- Car sales are improving
- Large banks able to extend credit

Minuses

- Weak May, neutral June
- Weak consumer confidence
- Credit still tight for small business
- Slow recovery in construction
- Possibility of European contagion

- Excluding non-economic factors the forecast shifts \$200 million from this biennium to the next



Questions



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